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## **CHILEAN RETAILERS: A UNIQUE MODEL IN LATIN AMERICA**

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### **ABSTRACT**

Latin America has experienced the arrival of U.S. and European retailers. However, retailing in Chile is 100% local, and differs from its neighbors. Chilean retailers have imitated the best practices of foreign retailers and through constant research and innovation in products and services are now internationalizing strongly through the region.

### **INTRODUCTION**

Retail globalization is increasing in Latin America. Recently, this part of the world has experienced the arrival of large American and European retail chains, such as Wal-Mart, Carrefour, and Casino, with their international expertise and vanguard technology. In Mexico, Argentina and Brazil, these foreign retail chains have become important leaders.

The retailing situation in Chile differs from other South American countries. The largest retail companies of grocery, department store, drugstore, and home improvement retailing, are all Chilean family businesses that compete strongly in this small market. This strong competition has hindered the internationalization attempts of large multinational retailers, such as Sears, J.C. Penney, Royal Ahold, Carrefour, and Home Depot, which withdrew from the market after poor performance.

Furthermore, Chilean retailers are gaining presence in Latin American markets. Chilean retailers such as Falabella, Cencosud, FASA, and Sodimac, have become familiar for consumers in Argentina, Peru, Colombia, and Mexico. By dealing with strong competition, Chilean retailers have imitated the best practices of foreign competitors and learned to adapt their retail offer to satisfy the local consumer's needs.

Research on international retailing has mainly looked at the internationalization attempts and experiences of retailers from developed markets (e.g., Sparks, 1995). However, there is still little understanding of how retailers from

emerging countries get strong enough to compete internationally.

Chilean retailers are led by professionals that belong to large family business groups. These firms are well regarded by the Chilean business community, and their top executives are legitimate. This paper suggests that Chilean retailers have improved their retail offer by imitating the best practices of the foreign retailers, and strengthening their market knowledge in order to constantly innovate in products and services. This formula has been successful for most of the retail sectors in Chile and has led to greater consolidation, concentration, professionalization, and internationalization of this retail industry.

### **LITERATURE REVIEW**

Due to increased internationalization of retailing, a vast amount of literature has emerged examining the international activities of European, North American, and Japanese retailers (e.g., Tordjman, 1988; Alexander, 1995; Robinson and Clarke-Hill, 1990; Treadgold, 1991; Sparks, 1995; Dupuis and Prime, 1996; Sternquist, 1997; Arnold and Fernie, 2000; Laulajainen, 1991; Goldman, 2001; Burt et. al., 2002). This research has been generally composed of internationalization attempts and experiences of retailers from developed countries.

Additionally, recent studies have looked at failed attempts from large multinational retailers in Latin America (e.g., Wrigley and Currah, 2002; Bianchi and Ostale, 2006), and the defensive actions of local retailers (e.g., Goldman, 2000; DaRocha and Dib, 2002; Bianchi and Mena, 2004). However, little is known about how retailers from emerging markets internationalize and compete in foreign markets.

Chilean retailers are gaining international presence in the Latin American region competing with huge companies such as Wal-Mart, Carrefour and Casino. As scholars argue that there is still a need for a better understanding of the internationalization process of retailers, the objective of this paper is to address these issues by examining the retail industry from an emerging market such as Chile.

### **CHILEAN RETAIL MARKETPLACE**

The retail marketplace in Chile is very competitive mainly because of Chile's capitalist economic system and openness to international trade due to political stability. The retailing

industry in Chile represents 26% of the nation's GDP for 2005, with sales of US\$29.800 million (Camara de Comercio de Santiago, 2006). This might seem modest compared to other countries in Latin America, such as Argentina, Mexico and Brazil, where retail sales go from US\$ 60.000 millions to US\$ 120.000 millions per year. However, among all Latin-American countries, Chile shows the highest retail sales per capita with approximately US\$ 1.400 per year (A.C. Nielsen, 2005). Nevertheless, compared with developed economies, retail per capita is still low.

Retail firms in Chile have professionalized by incorporated modern technology, new merchandise, and better service as well as loyalty programs and credit cards for consumers. During the 90's, retail firms started to participate in the financial business with private label credit cards that injected growth and profitability to the retail business. With retail credit, lower income consumers had access to a wider assortment of quality products. All these advances are being developed especially by the largest retailers, which have contributed to the decline of smaller neighborhood stores and shops.

The Chilean retailing industry presents several unique characteristics compared to other countries in Latin America. Recent acquisitions within the industry has led to increasing concentration and efficiency, and in most cases the 3 largest retailers account for more than 50% of the market. Furthermore, Chilean retailers have gone through a strong expansion process by opening stores along the country, and through acquisition and alliances of cross related formats, specially department stores, home improvement, and grocery retailers. With these phenomena, retail chains in Chile have become multi-format and the market shows increasing signs of channel blurring, which means that consumers can find similar products in all different retail formats. Finally, Chilean retailers have already expanded internationally and according to the Chilean Chamber of Commerce, these firms contemplate large investments in 2006-2007 for international expansion plans mainly in Argentina, Peru, and Colombia, as well as developing or acquiring new or complementary retail formats (Camara de Comercio de Santiago, 2006).

### **Grocery Retailing in Chile**

The grocery sector is the most important distribution channel for the mass consumption products in Chile, with 2005 sales of approximately US\$6.000 millions, which

represents 24% of total retail sales (Asach, 2006). Grocery retailing has strongly concentrated in the last few years, with 63,3% of the market shared owned by only two retail firms: D&S and Cencosud (BCI Report, 2006). This differs from 1996, where 6 retail firms had 55.6% of the market. The first supermarket in Chile opened in 1957 under the brand Almac, and belonged to the company D&S. Almost two decades later, in 1975, Cencosud created the first hypermarket Jumbo in Santiago. During the 90s, grocery retailing began to grow steadily in terms of players, sales, and store quantity and surface, and services.

In 1998, the first foreign actor Carrefour entered the Chilean market by opening a hypermarket store in Santiago. This was followed by Disco-Ahold International Holdings N.V., which took control of Santa Isabel, a local grocery chain. To respond, both Cencosud and D&S developed an investment plan to defend their positions against these foreign firms. Cencosud invested in store openings of Jumbo hypermarkets, and D&S developed a new hypermarket format. In 2003, both Carrefour and Disco Ahold announced withdrawal from the Chilean market due to poor performance. Cencosud acquired Santa Isabel from Ahold, and D&S acquired the operation of Carrefour in Chile, thus the industry became 100% local. Concentration continued in this industry by Cencosud acquiring the grocery chains Las Brisas and Montecarlo, and Falabella, the largest department store chain in Chile, acquiring Supermercados San Francisco.

D&S is the largest grocery chain in Chile, and is owned by the Ibañez Family. Having developed mainly the traditional supermarket format through the ALMAC banner, in 1984 it introduced the discount supermarket format EKONO with great success. In 1997, D&S introduced the discount hypermarket format, under the LIDER banner, and a few years after D&S decided to bring all formats together under the LIDER banner. From 1998-2001, D&S focused on opening new stores and providing new services to customers, such as the Presto Credit Card, coffee shops and drugstore products inside the store. By the end of 2005, D&S owned 85 LIDER stores and participated in the shopping center and financial business in Chile with the credit card Presto. Additionally, D&S has lounged several new product lines and private brands (D&S Annual Report, 2005).

Another relevant actor is the hypermarket retailer JUMBO, which belongs to

the group Cencosud S.A. JUMBO was founded in 1982 by its current president and main shareholder Mr. Horst Paulmann, and was the first hypermarket in Chile. The internationalization of JUMBO's operations to Argentina started the same year and much effort was put in developing the Argentinean market. Later in 1998, Cencosud defended itself against Carrefour and D&S, and started to open new JUMBO stores. In addition it acquired the grocery chain Santa Isabel from Disco-Ahold and became the second largest player in the Chilean market. By the end of 2005, Cencosud operated 106 stores of Santa Isabel, 28 Jumbo Hypermarkets in Argentina and Chile, and showed consolidated sales of US\$ 2518 million, and profits of US\$ 102 millions (65% Chile and 35% Argentina), with an increase of 50% from the previous year (Cencosud Annual Report, 2005). The rest of the industry is composed of smaller grocery retail chains, such as San Francisco and Unimarc, which none of them represent more than 4% of the market.

### **Department Store Retailing**

Approximately US\$ 2.500 million correspond to department store sales (Camara de Comercio de Santiago, 2006). Three large chains dominate this industry, Falabella, Ripley and Paris, which are focused on the high and middle income segments. All three chains provide similar products and services for customers, are involved in the real state business, and operate in large shopping malls. The aggressiveness of the competition has hindered operating margins, putting pressure in expanding nationally and internationally. For example, Falabella has operations in Peru and Argentina, and opening soon in Colombia, and Ripley also operates in Peru. The three of them are public companies with their stocks being traded in the stock exchange market.

There are also some middle size stores operating in this market and they represent an indirect competition for the three big ones. They focus on the middle to low income segments and basically offer two kinds of products: clothes (60%) and house appliances (40%). Their strategy is to operate in downtown areas of the most important cities outside of Santiago, as opposed to large shopping malls. This is the case of companies as La Polar, Corona, Johnson's, Tricot and Hites.

Similar to the grocery industry, department stores also show concentration and internationalization. Large retailers are acquiring

other retailers to increase retail offer and be able to compete through economies of scale, branding, expertise and know how. Margins are going down and retailers need to be more efficient. To achieve this, retailers have gone through a process of professionalization and changing organizational structure to the new competitive scenario. Thus, family members are now part of the board of directors, and are hiring professional executives with retail experience as managers, and keeping costs as low as possible. In addition, department store credit business has become a key factor for the profitability of these firms. The financial business has become very relevant in mergers and alliances in order to generate value through the synergies, therefore increasing the competitiveness of the new company.

Falabella is the largest department store retailer in Chile, owned by the Solari family. It is the undisputable leader of the department store sector, the main credit card controller, and the main shopping mall owner. Consolidated sales (Chile, Argentina, Peru, and Colombia) for the year 2005 were US\$ 3.800 millions, which represents an 18,6% growth compared to 2004 (Falabella Annual Report, 2005). Falabella has diversified its product and service offering by incorporating services such as credit, travel agent service, insurance, wedding gift lists, and internet sales. Falabella is also participating in other companies such as FASA (20%), and recently opened the Bank Falabella. Credit is a fundamental part of Falabella's business, with their CMR credit card, which has more than 3.000.000 customers. At the end of the year 2005, Falabella operated 35 stores in Chile, 10 in Peru and 6 in Argentina ([www.falabella.cl](http://www.falabella.cl)).

Ripley is the second largest department store retailer in Chile and belongs to the Calderon family. The company was initially founded in 1956 as a men clothing store. In 1993, Ripley opened the largest department store in South America, with 14.000 sq. mt. in size, with the objective of focusing on higher income consumers. During 1998, Ripley starts operating in Lima, Peru, with one store, following the steps of Falabella. During the year 2002, Ripley developed its Bank Ripley, which offered credit to their customers. At the end of the year 2005, Ripley held 30 department stores in Chile, and 9 in Peru, with consolidated sales of US\$ 1.450 million for that year (Ripley Annual Report, 2005).

PARIS was founded in the year 1900, by the family group Galmes. During 90s, the firm went through a growth process with many store

openings all over the country, and in 2004 it was sold to Cencosud. Since then, Paris has gone through a rationalization process of costs and improvement in their logistics and information systems, which has led to an increase in profits. At the end of 2005, PARIS operated 22 stores in Chile (Cencosud Annual Report).

Several foreign retailers have attempted to operate in Chile. For example, Sears opened a store in Chile during the late 1970', and J.C. Penney's opened a store in 1995. Both retailers withdrew from Chile after experiencing poor results. In both cases, Chilean retailers took strong actions to defend their local market positions.

### **Home Improvement Retailing**

Sales of home improvement and construction materials in Chile for the year 2005 were estimated in U.S. \$ 4.000 millions, and 31% of the market belonged to the three largest home improvement retailers: Sodimac, Construmart, and Easy (BCI Report, 2005). The remaining 69% is composed of many smaller hardware stores. Sodimac Home Center and Easy are both mega retailers that offer consumers a wide product assortment for home improvement, repairs, and also general home merchandise. Other main competitors are Sodimac Constructor and Construmart, both characterized as big warehouses that offer mainly construction materials for construction firms and professionals.

Sodimac was the pioneer of home improvement and construction materials in Chile, and is the leader of this retail industry. The Home Center format was introduced 15 years ago by Sodimac. Previously, this industry consisted of small hardware stores, which sold mainly construction materials. Home Center offered consumers construction materials, as well as general products for the home. This new concept for the Chilean market was adapted from similar formats from the U.S. and Europe, and was quickly accepted by consumers. A few years later it was imitated by Cencosud with Easy.

From 1998-2001, Home Depot was the only foreign retailer in this industry, and offered a wide assortment of products for home improvement and do-it-yourself activities. Because of huge losses, Home Depot withdrew from Chile in 2001, and sold its shares to its local minority partner Falabella, which changed the name of Home Depot to Home Store and incorporated several changes that generated profits for the company. Nevertheless, in 2003, Falabella acquired Sodimac, and merged Home

Store into Home Center. Since then, Sodimac expanded internationally and in 2005 operates 54 stores in Chile, 2 stores in Peru and 9 stores in Colombia (Falabella Annual Report, 2005).

Easy, owned by Cencosud, is another relevant retailer in the industry of home improvement. Since 1998, Easy has gone through an ambitious plan to expand the amount of stores in Chile in order to compete against Home Depot and Sodimac. In addition, Easy has implemented a corporate credit card for consumers, and a wider product assortment in the stores, very much imitating the practices of Sodimac. In 2005, Cencosud operated 18 Easy stores in Chile and 26 stores in Argentina ([www.cencosud.cl](http://www.cencosud.cl)).

### **Drug Store Retailing**

During 2005, total sales for this retail sector in Chile were approximately US\$ 1.000 millions (El Mercurio, 2006). Three large retailers have more than 90% of the market share: FASA (25%), SalcoBrand (28%), and Cruz Verde (34%). Drug store retailing has evolved during the last decade towards a drug store format, and drug retailers offer a wide selection of pharmaceuticals, body care, and food items, along with parking space, technology, and loyalty card, imitating pharmaceutical chains in the U.S. such as Walgreen. Competition is very strong in this industry, and margins have fallen 15% to 20% since 2004, due to price wars. These players have made important adjustments inside their firms and expansion plans to regional cities in order to compete.

FASA is the largest drug store chain in Latin America with consolidated sales of US\$ 1200 millions (FASA Annual Report). It was founded by Jose Codner in 1968, and in 2005 has presence in Chile, Peru, and Mexico with over 930 stores. In 1996, FASA opened in Peru as Boticas FASA, and in 1997 opened to the stock market. In 1999 Falabella acquired 20% of FASA. Later in 2000, FASA entered the Brazilian market, however was not able to operate profitable so it withdrew from this market at the end of 2005. During 2002, FASA took control of the Mexican retailer Farmacias Benavides, and has done very well in this market. FASA has an alliance with Falabella for using CMR credit card. By the end of 2005, FASA operated 909 drug stores in Chile, Peru and Mexico ([www.fasa.cl](http://www.fasa.cl)).

SalcoBrand is the fusion in 1999 of two pharmacy family business, and has 290 stores in Chile with a loyalty card which provides several benefits to clients. During 2003, it introduced a

new convenience store format OK Market, and both formats expand together. Cruz Verde operates more than 400 stores in Chile, and is the retailer with the largest market share in stores due to the franchising expansion strategy in Chile. Farmalider was born in 2001 to D&S. By the end of 2005, the retailer accounted to a market share of 5 % and 67 stores, most located inside LIDER stores ([www.dys.cl](http://www.dys.cl)).

## DISCUSSION AND CONCLUSIONS

The previous analysis shows that the Chilean retailing industry at 2005 has several distinguishing characteristics from its neighboring countries. Threats from foreign firms and intense competition have resulted in a local industry with increased level of consolidation, concentration, and professionalization. Most large retailers participate in diverse retail industries, and with a wide product and service offer. Additionally, large retailers have started to expand nationally and internationally.

All the retail sectors examined are very concentrated, and the 2-3 major players represent a large portion of market share. Other players are smaller chains, which mainly have presence in regions outside of the capital. Santiago concentrates most of the businesses and population in Chile. However, due to intense competition in Santiago, retailers are opening stores outside of the capital and looking for growth in other cities in Chile, which generates threats to smaller regional retailers.

Another trend of this retail market is the growth of multi-format retail firms. This means that the same retail group participates in different retail sectors by developing new formats or acquiring complementary ones. For example, grocery retailer Cencosud owns shopping centers, and developed the home improvement format Easy, and later acquired department store retailer PARIS. Similarly, Falabella also owns shopping malls, drug store retailer FASA, and acquired home improvement Sodimac and grocery chain San Francisco. This phenomenon results in strong retail holdings that block-out the competition in several fronts. These retailers make the most of operational synergies in terms of costs, logistics, strategic locations, credit, and loyalty programs.

A final trend of this industry is the strong internationalization to Latin-America. In all retail sectors analyzed, the main retail chains have operations abroad. For example, Falabella operates in Argentina, Peru, and Colombia. Cencosud operates Jumbo and Easy stores in

Argentina. Sodimac operates in Colombia and Peru, and FASA operates in Peru and Mexico. Cencosud is acquiring grocery chain Disco in Argentina which would make Cencosud the main grocery retailer in this country. Cencosud has also announced its interest in internationalizing to Brazil and Colombia.

Most retail internationalization attempts have been successful, and large Chilean retailers have plans of further national and international expansion. Some prefer to look for new markets and others to strengthen and expand in actual markets. This has led Chilean retailing to be positioned among the largest in Latin America. We conclude that this retail industry is characterized by excellent know how, expertise, and permanent innovation. All this summed with a good political and economic situation in Chile provides stability, results in an industry with high potential to continue its growth process.

International retailer's experience and practices in Chile were useful for the Chilean retail industry. Local firms learned much from foreign retailers that operated in Chile, especially regarding management practices and technology. The threat of multinational companies coming to such a small market like Chile led local retailers to defend themselves aggressively through an understanding of these companies' strategies around the world. For example, Carrefour's and Wal-Mart's big hypermarkets formats and low prices have been the motto for D&S growing strategy along the country. Home Depot's do-it-yourself concept was copied and successfully implemented with a local touch by Sodimac in Chile, long before the international company decided to come into the local market.

Furthermore, international retailers operating in Chile gave local firms the opportunity to learn new concepts of the industry, such as logistics, consumer service, technology, and merchandising, among others. This explains how local retailers from all sectors have taken advantage by using the tools developed by international retailers. These firms have learned to mimic best practices without losing their identity, through highlighting local values and traditions, and hiring local and well respected managers. In addition, domestic retailers and managers have learned to deal with foreign competitors with deep resources, and this has led to stock openings, alliances, and acquisitions. As a result, retailing has become an important industry which translates in increased research, graduate programs, more conferences and retail events, and more labor force demanded by these firms.

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